



## AMERICANS ARE FEELING THE PAIN OF THE IRS BACKLOG

If you are an American taxpayer, there is a good chance you have had a problem with the Internal Revenue Service (IRS) over the past two years. With the 2023 tax filing deadline fast approaching, millions of unprocessed returns from previous filing seasons remain backlogged.<sup>1</sup> Meanwhile, taxpayers are lucky to receive a response if they attempt to contact the IRS to resolve a problem, as only 13 percent of calls were answered by an IRS representative in fiscal year (FY) 2022.<sup>2</sup>

The first portion of the IRS's stated mission is to "provide America's taxpayers top quality service by helping them understand and meet their tax responsibilities." Instead, however, the Biden Administration's IRS has focused on ways they can audit more Americans, while blaming their backlog on a lack of resources.<sup>3</sup> Meanwhile, the website of the Taxpayer Advocate Service (TAS) office – the independent organization within the IRS tasked with helping taxpayers resolve problems – noted in its latest report that "the bad news is that taxpayers and tax professionals experienced more misery in 2022."<sup>4</sup>

### BACKGROUND

Experiencing headaches when paying your taxes is nothing new, but the COVID-19 pandemic exposed and exacerbated many problems and inefficiencies at the IRS. Many of the current backlog problems arose due to months-long IRS office closures, rendering those offices unable to process mailed correspondence and returns. Simultaneously, Congress enacted legislation that expanded the responsibilities of the IRS tremendously during the pandemic. Since then, the IRS has compounded its backlog problems in various ways. The IRS backlog crisis is not due to lack of funding, since the IRS began FY2022 with more than \$1.4 billion in unspent funds.<sup>5</sup> Furthermore, the IRS received an increase in funding of nearly 6% in FY2022 appropriations.<sup>6</sup>

The TAS's Annual Report to Congress identified the most serious problems encountered by taxpayers as:<sup>7</sup>

- **Communication with the IRS has been slow or nonexistent as problems remain.**
  - Since the IRS tries to process returns on a first-in, first-out basis, they spent much of 2022 working through tax returns filed as far back as April 2021.<sup>8</sup>
  - Calls to customer service representatives are unlikely to get a response, with only 22 million of 173 million calls being answered in FY2022.<sup>9</sup>
  - The time spent on hold waiting to talk with a representative also ticked up to an average of 29 minutes in FY2022.<sup>10</sup>
  - After millions of "math error" notices, the IRS took an average of 193 days, or over 6 months, to respond to taxpayers.<sup>11</sup>
- **The IRS continuously creates new problems and then back tracks.**
  - Despite the IRS's incredibly slow response time, taxpayers could still be subject to late fees, interest, and delinquency warnings due to a problem of the IRS's creation.<sup>12</sup>
  - While taxpayers and practitioners were already struggling to successfully pay their taxes given the lack of communication from the IRS, the IRS decided to increase hurdles for tax preparation by requiring a taxpayer's identification to be verified through ID.me, which used a process that included facial recognition.<sup>13</sup> The IRS added an alternative to this requirement a few months after launching following bipartisan backlash.<sup>14</sup>

- In addition, the Biden Administration proposed requiring banks and other financial institutions to report to the IRS the amount of money going in and out of an account if the amount exceeded \$600 in a year.<sup>15</sup> Senate Democrats then attempted to raise the reporting threshold to \$10,000 and finally backed down from the proposal altogether after significant pushback.<sup>16</sup>
- The IRS also created a new child tax credit portal for individuals who do not normally file a return, which was promoted by the White House. In early March 2022, the portal was suddenly taken offline after confusion over who should be using the portal, and what the White House suggested may cause “chaos” at the IRS if left online. Instead of using the portal, the Biden Administration now suggests low-income earners who traditionally do not fill out a tax return to fill one out if they want to receive their money before April 15. Otherwise, they will need to wait until the portal reopens on April 18.<sup>17</sup>
- The IRS created new international reporting requirements for many pass-through entities despite the instructions continuing to evolve and an inability to electronically file the forms before the due date.<sup>18</sup>

## **POLICY SOLUTIONS**

Although the IRS has taken some action since congressional Republicans pressed for the backlog reduction, more needs to be done, whether by the IRS or through congressional action.<sup>19</sup>

### **In the short-term, the following changes should be made:**

- Don’t punish taxpayers because of the IRS’s delays.
  - Provide targeted penalty relief for taxpayers who claimed an employee retention tax credit (ERTC) for 2020 or 2021 but have not received a refund and are expected to pay taxes this filing season on money they have not received.
  - Even if taxpayers mailed responses or filed an amended return on time, the IRS proceeded to send additional letters and notices because taxpayers’ correspondence is not being processed in a timely manner. The IRS should delay the collection process for filers until any active and pending penalty abatement requests have been processed, as recommended by the TAS.<sup>20</sup>
  - Pause audits and other notices that require taxpayer correspondence and repurpose as much personnel as possible to decrease the backlog.
- While Congress has given additional hiring flexibility to the IRS in its latest funding bill, more administrative reforms are needed to improve federal agency hiring processes.
  - H.R. 6967, the Chance to Compete Act, would help improve the federal hiring process by allowing agencies to hire more easily based on skills and experience, rather just what degrees an applicant has.<sup>21</sup> The bill would codify and build upon Trump-era reforms to modernize the federal hiring process.<sup>22</sup>
- Apply a consistent mailbox rule deadline to electronically submitted payments
  - Current law allows checks mailed by taxpayers to the IRS to be treated as timely if the mail is postmarked before the deadline.<sup>23</sup> Unfortunately, electronic payments sent through Treasury’s Electronic Federal Tax Payment System must be made the night before the deadline at 8:00 PM to be considered timely.<sup>24</sup> Therefore, taxpayers may be incentivized to mail a check rather than pay online, which adds to the IRS’s paperwork burden.
  - Congress should ensure the deadlines are consistent and pass H.R. 3278 to codify these changes.<sup>25</sup>
- Prioritize any new IRS funding and hiring to be for taxpayer services over tax enforcement while the IRS is struggling to clear the backlog from previous tax filing years.
  - While Democrats gave \$80 billion to the IRS, with over half of that amount going to increased enforcement, IRS staff complained about a lack of basic resources, such as staplers and carts for filing purposes.<sup>26</sup>
  - As long as returns from previous filing years remain unprocessed, it will be incredibly difficult for taxpayers to file their next return.
  - Although Congress directed new dollars to taxpayer services in the recently passed government funding legislation, the amount still made up less than half of the increase in funding for the IRS with an

identical mount going toward enforcement.<sup>27</sup>

- Delay the new Form K-2 and K-3 reporting requirements until electronic filing is fully available.<sup>28</sup>
  - The IRS released the forms and draft instructions for the new international reporting requirements for pass-through entities in June 2021. However, the IRS then updated the instructions in January 2022, just a few short months before the filing deadline.
  - To make matters more complicated, electronic filing for the new forms will not be available until after the filing deadline.<sup>29</sup> Tax preparation services companies that file 250 or more returns a year are required to electronically file, though.<sup>30</sup> Therefore, these businesses would all need to file an extension.
  - The IRS provided some relief in February to allow filers to allow a pdf attachment for smaller partnerships with 50 or less partners or shareholders, but this relief is insufficient considering pdf attachments often go “missing” when the IRS lacks the bandwidth to process and review them.<sup>31</sup>
- Increase the interest rate for delayed refunds to account for inflation.<sup>32</sup>
  - The IRS currently pays an interest rate of 3% to taxpayers on their delayed refunds even as inflation soared to 7.9% in February.<sup>33</sup> Therefore, as taxpayers wait around for the IRS to issue a refund, the value of their money is weakened, preventing the ability to receive higher returns elsewhere.<sup>34</sup>
  - While interest on delayed refunds is taxpayer money that should never have to be spent, taxpayers should not be held financially responsible due to the government’s own inefficiency.

**To help the IRS work more effectively for taxpayers moving forward, the following should be done:**

- Once the backlog has cleared, the IRS should prioritize IT modernization.
  - Despite decades-long complaints about faulty and outdated equipment, the IRS continues to fail to successfully complete updates to its systems despite continued funding for modernization from Congress. Americans for Tax Reform compiled reports on the IRS’s numerous attempts to modernize its 60-year-old system, which may now not be completed until 2030.<sup>35</sup>
  - Some forms are still manually processed but should be digitized, such as amended tax returns.<sup>36</sup>
- Provide improved communication tools and transparency of the status of tax returns.
  - Historically, the IRS has only allowed taxpayers to communicate digitally when conducting an audit or performing collections.<sup>37</sup>
  - Although the IRS has begun to use a new virtual assistant to resolve taxpayer inquiries, the virtual assistant remains too limited in scope.<sup>38</sup>
  - The IRS should expand the use of digital tools to allow agents to remain focused on more complex issues.

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<sup>1</sup> National Taxpayer Advocate Annual Report to Congress: 2022. Internal Revenue Service <https://www.taxpayeradvocate.irs.gov/reports/2022-annual-report-to-congress/>

<sup>2</sup> Most Serious Problem #3: Telephone and In-Person Service. National Taxpayer Advocate Annual Report to Congress: 2021. Internal Revenue Service. [https://www.taxpayeradvocate.irs.gov/wp-content/uploads/2022/01/ARC21\\_MSP\\_03\\_Telephone.pdf](https://www.taxpayeradvocate.irs.gov/wp-content/uploads/2022/01/ARC21_MSP_03_Telephone.pdf)  
<https://www.taxpayeradvocate.irs.gov/reports/2022-annual-report-to-congress/full-report/>

<sup>3</sup> The Agency, its Mission and Statutory Authority. Internal Revenue Service. <https://www.irs.gov/about-irs/the-agency-its-mission-and-statutory-authority> and Treasury and IRS Announce Aggressive Plan to End Pandemic Inventory Backlog This Year. U.S. Department of the Treasury. March 10, 2022. <https://home.treasury.gov/news/press-releases/jy0648>

<sup>4</sup> National Taxpayer Advocate Annual Report to Congress: 2022. Internal Revenue Service <https://www.taxpayeradvocate.irs.gov/reports/2022-annual-report-to-congress/>

<sup>5</sup> GOP Letter: IRS Must Provide Plan to Address More Than 16 Million Outstanding Tax Returns. U.S. Committee on Ways and Means. January 19, 2022. <https://gop-waysandmeans.house.gov/gop-letter-irs-must-provide-plan-to-address-more-than-16-million-outstanding-tax-returns/>

<sup>6</sup> P.L. 117-103

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